

VZCZCXRO3224
RR RUEHDE RUEHLMC
DE RUEHLM #0346/01 0950654
ZNR UUUUU ZZH
R 040654Z APR 08
FM AMEMBASSY COLOMBO
TO RUEHC/SECSTATE WASHDC 7964
INFO RUCPDOG/USDOC WASHDC
RUEHAD/AMEMBASSY ABU DHABI 0458
RUEHNE/AMEMBASSY NEW DELHI 1942
RUEHKA/AMEMBASSY DHAKA 0819
RUEHDO/AMEMBASSY DOHA 0236
RUEHIL/AMEMBASSY ISLAMABAD 7812
RUEHKT/AMEMBASSY KATHMANDU 5995
RUEHGP/AMEMBASSY SINGAPORE 5725
RUEHBK/AMEMBASSY BANGKOK 3390
RUEHKP/AMCONSUL KARACHI 2336
RUEHCG/AMCONSUL CHENNAI 8419
RUEHDE/AMCONSUL DUBAI 0140
RUEHGV/USMISSION GENEVA 2697
RUEHC/DEPT OF LABOR WASHDC
RUEATRS/DEPT OF TREASURY WASHDC
RUEHLMC/MILLENNIUM CHALLENGE CORPORATION

UNCLAS SECTION 01 OF 03 COLOMBO 000346

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STATE FOR SCA/INS AND EEB/TRA/OTP
STATE PASS USTR, DOL/ILAB FOR TINA MCCARTER
NEW DELHI, SINGAPORE AND BANGKOK FOR FAA AND TSA

E.O. 12958: N/A

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SUBJECT: SRI LANKA RESUMES MANAGEMENT OF NATIONAL CARRIER AND
APPOINTS FINANCE SECRETARY AS BOARD CHAIRMAN

REF: A. COLOMBO 47 B. 07 COLOMBO 394

1. (SBU) Summary and comment: The government of Sri Lanka resumed management control of the national carrier Sri Lankan Airlines on April 1. The government has appointed Treasury Secretary (and mastermind of the Sri Lankan economy) P.B. Jayasundera to be chairman of the Sri Lankan Board of Directors. Jayasundera replaces local tycoon Harry Jayawardena, who had clashed with Emirates management. The appointment is intended to generate confidence that the airline will be managed in a financially prudent manner, and also to improve relations with Emirates, which still owns 44% of Sri Lankan shares and three of the seven seats on the board. The Secretary of Ports and Aviation assured us that the airline will

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have "complete commercial flexibility without government interference" but President Rajapaksa's statement that the national carrier "must be used in a more dynamic and enterprising manner to further the goals of the country" suggests that the government won't be entirely hands-off.
End summary and comment.

SRI LANKA RESUMES CONTROL OF NATIONAL CARRIER,
RESHUFFLES BOARD OF DIRECTORS

2. (SBU) National carrier Sri Lankan Airlines reverted to Sri Lankan government management control on April 1, with the termination of a 1998-2008 management contract held by Emirates Airlines (ref A). The government of Sri Lanka owns 51% of the airline's shares, Emirates owns 44%, and airline employees own the remaining 5% of shares. On March 28, President Rajapaksa replaced three of the four Sri Lankans on the airline's seven-member board of directors, appointing Treasury Secretary P.B. Jayasundera as the new chairman. (Note: Jayasundera was treasury secretary and chairman of the Public Enterprise Reform Commission in 1998 when the government partially privatized the unprofitable airline with the share sale and management contract to Emirates. The deal was regarded at the time

as having been corrupt -- there was speculation that then-President Kumaratunga profited personally from steering the deal toward Emirates.) A senior minister told Ambassador that the Jayasundera appointment was temporary until a suitable private sector figure could be selected. He expected Jayasundera to mend relations with Emirates, after former chairman and local conglomerate tycoon Harry Jayawardena had had a personality clash with Emirates President Tim Clark.

13. (SBU) The other new Sri Lankan board members are Lalith De Silva, a former telecom CEO whom the government had engaged as a consultant to work on the transition from Emirates; and Sunil Wijesinghe, a respected businessman and management consultant, currently chairman of Dankotuwa Porcelain Ltd., and brother-in-law of Central Bank Governor Nivard Cabraal. Remaining on the board are Nishantha Wickremasinghe, appointed in 2006, brother-in-law of President Rajapaksa; and three senior Emirates managers based in Dubai.

NO CEO; STAFF JUMPING SHIP

14. (SBU) Sri Lankan lacks a CEO however. When Emirates announced its pull-out, the airline elevated its communications director, Chandana de Silva, to temporarily fill the CEO slot. However de Silva recently left the position to join Emirates. The government is advertising the opening for the CEO position. Thirty of the airline's 200-plus pilots have also left. A group of senior pilots we spoke to emphasized that pilots were leaving simply because other airlines were offering them more money, not because they lacked confidence in Sri Lankan's business prospects.

GOVERNMENT SAYS IT WON'T INTERFERE IN MANAGEMENT...

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15. (SBU) Secretary of Ports and Aviation Tilak Collure told EconOffs and visiting Federal Aviation Administration representative from Embassy New Delhi that, back under national management, the airline will have "complete commercial flexibility without government interference." The pilots we spoke to likewise said they did not expect the new management to enact any big changes in the short term. Collure said it was possible the government would at some point allocate funds to the airline to support its operations. (Note: Sri Lankan as a whole is currently barely profitable, having made \$7.8 million in 2007 with revenue from ground handling and ancillary operations covering losses in flight operations.) The pilots pointed out that the airline needs additional planes in order to expand routes, but lacks the cash to purchase any.

16. (SBU) Collure and others we talked to also downplayed widespread speculation that Sri Lankan Airlines would come to the rescue of ailing national budget airline Mihin Air (ref B). Collure told us the government's position was that "Mihin will have to stand on its own," but that "if there are ways to cooperate, so be it" According to news reports, the airline has been losing a few million dollars each month as a result of using expensive wet-leased planes and inefficient overall operations. Mihin's head of flight operations told Econoff that "60-70% of media reporting" is incorrect, but did not contend that the airline is making money. He admitted that a merger had been discussed but rejected by the former Sri Lankan board, but might again be considered by the new board.

... BUT PRESIDENT SAYS AIRLINE MUST
"FURTHER THE GOALS OF THE COUNTRY"

17. (SBU) Collure's assertions of Sri Lankan's independence notwithstanding, President Rajapaksa stated in a paid advertisement in local newspapers that the national carrier "must be used in a more dynamic and enterprising manner to further the goals of the country." Sri Lankan's new marketing campaign reflects the kind of inward-looking approach common to other state-owned enterprises under the Rajapaksa government. The airline is serving Sri Lankan national food to celebrate the new domestic management control. It is seeking to drum up business by offering discount fares to Sri

Lankans traveling abroad to visit relatives and Sri Lankans abroad returning to visit relatives. The government also announced that it will use Sri Lankan Airlines for all official travel abroad of both working level government officials and government VIPs.

¶8. (SBU) The government has also indicated that the separation between Sri Lankan and Mihin won't be as complete as Collure stated. Presidential Secretary Lalith Weeratunga told the government-run Daily News that there would be not a merger but a "partnership" between the airlines. The Daily News reported that "a corporate plan was being drawn out between the two airlines with the proposal of drawing out the operational synergies and how both could be maintained in tandem with each other as a partnership in terms of Human Resources and Finances."

COMMENT: NEW CHAIRMAN IS A MIXED BLESSING;
PRESIDENT BRACING FOR FAILURE?

¶9. (SBU) P.B. Jayasundera is the fiscal mastermind keeping Sri Lanka's sprawling and wasteful government from going broke. With his fiscal management skills, he will likely be more capable than most other political appointees would be at holding down Sri Lankan Airlines' expenses. On the other hand, he shares President Rajapaksa's vision of a paternalistic government whose state enterprises advance populist, but costly, economic policies. So he will not likely resist give-aways like the reduced fares for Sri

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Lankans flying the national carrier. In this sense he is far from the professional manager the airline needs. He has other liabilities as well. He is extremely busy running the Treasury and Finance Ministry, so will not be able to devote full-time attention to the airline. His proximity to various deals alleged to have been corrupt also raises concerns.

¶10. (SBU) The Rajapaksa government is trying to put a positive nationalist face on the airline's reversion to Sri Lankan management. Indeed, critics contend that the original deal with Emirates had been too generous and that Emirates had exploited more than enhanced Sri Lankan Airlines. It is true that Emirates did not invest in Sri Lankan the way it has in its own brand, but it definitely managed the airline more effectively than the government had. Government management of state enterprises has long been poor in Sri Lanka, so the country appears likely to lose from Emirates' departure. President Rajapaksa himself sounded pessimistic when he told Sri Lankan Airlines employees April 3: "If the company fails in today's fiercely competitive airline business of the world and the region in particular, especially at a time there is a global economic recession, you ought to blame yourselves for it."
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